Equity Research

March 18, 2021

BSE Sensex: 49217

**ICICI Securities Limited is the author and distributor of this report**

**Company update**

## Oil & Gas

**Target price: Rs544**

### Earnings revision

| (%) | FY21E | FY22E |
|---|---|---|
| Sales | ↑ 9.7 | ↑ 42.4 |
| EBITDA | ↑ 37.9 | ↓ 6.0 |
| EPS | ↑ 61.1 | ↑ 14.0 |

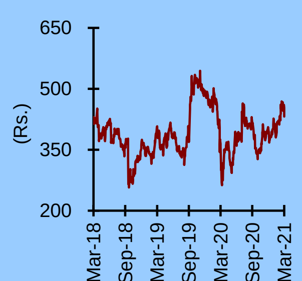
### Target price revision

Rs544 from Rs423

### Shareholding pattern

| | Jun '20 | Sep '20 | Dec '20 |
|---|---|---|---|
| Promoters | 53.0 | 53.0 | 53.0 |
| Institutional investors | 32.4 | 32.5 | 31.5 |
| MFs and others | 13.7 | 13.8 | 13.2 |
| Banks / FIs | 0.1 | 0.1 | 0.1 |
| Insurance Cos. | 6.7 | 6.7 | 6.7 |
| FIIs | 11.9 | 11.9 | 11.5 |
| Others | 14.6 | 14.5 | 15.5 |

### Price chart





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**INDIA**

# Bharat Petroleum Corporation

**BUY**
**Maintain**
**Rs427**

## Privatisation bid and GRM key to outlook

**We resume our coverage on BPCL with BUY rating and target price of Rs544/share (27% upside). Our target price of Rs544 assumes successful bid price in privatisation of Rs609/share (8x FY22E EV/EBITDA) on 56% of investors' holding and Rs462/share (6x FY22E EV/EBITDA) on balance. We estimate FY22E core GRM recovering to US$3.5/bbl from US$1.5/bbl in 9MFY21, but net marketing margin fall to Rs2.5/l from Rs3.07/l in FY21E. We expect global demand recovery and refinery closures to drive GRM recovery. Net marketing margin is Rs0.09/l now, but we are hopeful of price hikes/excise cut boosting net margin to Rs2.5/l.**

- **Raise FY21-FY22E EPS and target price**: We have raised our FY21E EPS (up 250% YoY) by 61% due to: 1) Factoring product inventory gain of Rs47.6bn (Rs24.2bn in 9M and Rs23.4bn in Q4E) vs nil earlier; 2) upgrade in net auto fuel marketing margin to Rs3.07/l from Rs2.5/l earlier; and 3) cut in interest cost by 55% to factor in the steep fall in 9M. We have also raised our FY22E EPS estimate by 14% due to 1) upgrade in net marketing margin to Rs2.5/l vs Rs2.25/l earlier and 2) cut in interest cost by 46% as NRL stake sale and treasury shares sale reduce debt. FY22E EPS including inventory gain would be down 24% YoY, but that excluding would be up 34% YoY. Our target price of Rs544 (up 27%) assumes 56% of holding realises Rs609 (8x FY22E EV/EBITDA vs FY21E earlier) in successful bidder's open offer and Rs462 (6x FY22E EV/EBITDA) is realised on balance. **FV will be higher at Rs628 if successful bid price is Rs759 (EV based on Essar Oil deal).**
- **Singapore GRM at 6-quarter high but not out of the woods; demand recovery & refinery closures key to recovery:** Reuters' Singapore GRM, which touched a low of minus US$0.9/bbl in Q1FY21, has recovered to 6-quarter high of US$1.9/bbl in Q4FY21-TD. Recovery in global oil demand from lows and snowstorms that led to plunge in US refinery utilisation to 56-76% from 83% and product inventories have boosted GRM. Petrol cracks are at 5-quarter high but diesel cracks are well below pre-covid levels. Second wave of covid reversed demand recovery especially in Europe and jet fuel demand is still sharply below pre-covid levels. However, we are optimistic that further demand recovery driven by vaccine rollout and global refinery closures (1.5m b/d to be shut and another 1.4m b/d may shut) will boost global refinery utilisation from 38-year low of 72.4% to 77.4% in CY21E and drive up GRM.
- **Marketing margin at record high in FY21E; price hikes/excise to drive rise from current lows:** Net auto fuel marketing margin is at Rs3.19/l in FY21-TD but very low at Rs0.09/l on 18-Mar'21 and minus Rs0.16/l on 1-Apr'21E. We expect price hikes and/or excise cuts that are not passed on to ensure net margin at ~Rs2.5/l in FY22E. Our optimism is due to: 1) Healthy auto fuel marketing margin being crucial to success of BPCL's privatisation; 2) FY22E budget excise estimate leaves room to cut excise duty by Rs8.5/l and 3) this government's track record. Net marketing margin was Rs0.96-1.07/l in first four years of this government's tenure (FY15-FY18) and Rs1.83-2.22/l in FY19-FY20. Price hikes were made to keep net margins at a reasonable level even when oil surged to US$86/bbl and INR weakened to Rs75 in Oct'18, seven months before 2019 elections.

| | |
|---|---|
| Market Cap | Rs927bn/US$12.7bn |
| Reuters/Bloomberg | BPCL.BO/BPCL IN |
| Shares Outstanding (mn) | 2,169.3 |
| 52-week Range (Rs) | 469/263 |
| Free Float (%) | 47.0 |
| FII (%) | 11.5 |
| Daily Volume (US$'000) | 66,827 |
| Absolute Return 3m (%) | 8.4 |
| Absolute Return 12m (%) | 28.4 |
| Sensex Return 3m (%) | 4.8 |
| Sensex Return 12m (%) | 70.5 |

| Year to Mar | FY19 | FY20 | FY21E | FY22E |
|---|---|---|---|---|
| Revenue (Rs mn) | 34,08,792 | 32,97,972 | 23,09,852 | 34,11,328 |
| Net Income (Rs mn) | 78,023 | 37,360 | 1,27,414 | 97,071 |
| EPS (Rs) | 39.7 | 16.8 | 58.7 | 44.7 |
| % Chg YoY | -13% | -58% | 250% | -24% |
| P/E (x) | 10.8 | 25.4 | 7.3 | 9.5 |
| CFPS (Rs) | 56.0 | 35.7 | 117.0 | 62.3 |
| EV/E (x) | 8.7 | 23.3 | 5.1 | 8.8 |
| Dividend Yield (%) | 3% | 1% | 7% | 3% |
| RoCE (%) | 15% | 5% | 18% | 12% |
| RoE (%) | 21% | 8% | 44% | 16% |

**Please refer to important disclosures at the end of this report**

# Resume coverage with BUY rating

## Raise FY21-FY22E EPS and target price; retain **BUY**

**We resume coverage on BPCL with a BUY rating and target price of Rs544/share (27% upside).**

### Raise FY21E EPS by 61% to factor in 9MFY21 EPS & Q4 outlook

We have raised BPCL's FY21E recurring EPS estimate by 61% mainly due to:

- Factoring product inventory gain of Rs47.6bn vs nil earlier. BPCL's 9MFY21 product inventory gain was Rs24.2bn and we estimate Q4 gain at Rs23.4bn.
- Estimating auto fuel net marketing margin at Rs3.07/l vs Rs2.5/l earlier. Net margin is at Rs3.19/l in FY21-TD and at Rs0.09/l on 18-Mar'21, which we are assuming will remain the same in the rest of FY21E.
- Cut in interest cost by 55% (Rs18.1bn) to Rs14.8bn from Rs32.9bn earlier. Interest cost stood at Rs11.4bn in 9MFY21 and Rs3.45bn in Q3FY21.

The upgrade in FY21E EPS is despite cutting FY21E GRM to US$3/bbl from US$4.5/bbl earlier and crude throughput estimate from 27.2mmt earlier to 25.8mmt.

**Table 1: FY21E EPS estimates raised by 61% and FY22E by 14%**

| | FY21E | FY22E |
|---|---|---|
| **BPCL's consolidated recurring EPS** | | |
| Revised estimate | 58.7 | 44.7 |
| Earlier estimate | 36.5 | 39.3 |
| **Change** | **61%** | **14%** |

Source: Company data, I-Sec research

### Debt down by Rs172bn in 9MFY21; to fall further in Q4FY21

BPCL's debt is down by Rs172bn from Rs419bn in Mar'20 to Rs247bn in Dec'20. Debt is expected to decline further in Q4FY21 due to Rs98.8bn, it is likely to raise from stake sale in NRL and funds raised from sale of treasury shares.

### FY21E EPS up 250% YoY boosted by marketing and inventory gains

BPCL's 9MFY21 recurring consolidated EPS is up 114% YoY. We estimate its standalone Q4FY21E recurring profit at Rs27.1bn vs recurring loss of Rs0.9bn in Q4FY20. We estimate BPCL's FY21E recurring consolidated EPS to be up 250% YoY driven by:

- 38% YoY rise in auto fuel net marketing margin to Rs3.07/l.
- Product inventory gain of Rs47.6bn vs loss of Rs38.0bn in FY20
- Reported standalone GRM of US$3/bbl vs US$2.5/bbl in FY20

### Raise FY22E EPS by 14% on higher marketing margin & interest cut

We have raised BPCL's FY22 EPS estimate by 14% mainly due to:

- Estimating auto fuel net marketing margin at Rs2.5/l vs Rs2.25/l earlier.
- Cut in interest cost by 46% (Rs15.8bn) to Rs18.4bn from Rs34.2bn earlier.

**Table 2: FY21E EPS up 250% YoY while that in FY22E down 24% YoY**

| | FY19 | FY20 | FY21E | FY22E |
|---|---|---|---|---|
| **Consolidated recurring EPS** | **39.7** | **16.8** | **58.7** | **44.7** |
| YoY change | -13% | -58% | 250% | -24% |
| **Core GRM (US$/bbl)** | **4.02** | **4.24** | **1.03** | **3.50** |
| YoY change | -33% | 5% | -76% | 239% |
| **Reported GRM (US$/bbl)** | **4.58** | **2.50** | **3.01** | **3.50** |
| YoY change | -33% | -45% | 20% | 16% |
| **Crude throughput (mmt)** | **31.0** | **31.9** | **25.8** | **32.0** |
| YoY change | 9% | 3% | -19% | 24% |
| **Auto fuel net marketing margin (Rs/l)** | **1.83** | **2.22** | **3.07** | **2.50** |
| YoY change | 73% | 21% | 38% | -19% |
| **Domestic sales volume (mmt)** | **43.1** | **43.1** | **38.6** | **44.6** |
| YoY change | 10% | 0% | -10% | 16% |
| **Product inventory gain/loss (RS-bn)** | **1.7** | **(38.0)** | **47.6** | **0.0** |
| YoY change (Rs-bn) | 0.5 | (39.8) | 85.6 | (47.6) |

Source: Company data, I-Sec research

## FY22E EPS down 24% YoY; excluding inventory gain up 34% YoY

We estimate BPCL's FY22E EPS being down 24% YoY mainly due to no inventory gain assumed in FY22E vs product inventory gain of Rs47.6bn and crude inventory gain of US$2/bbl in FY21E. However, if inventory gain is excluded from FY21E EPS, FY22E EPS will be up 34% YoY.

## Raise target price by 29% to Rs544; based on FY22E EBITDA vs FY21

We have raised our target price by 29% to Rs544/share (27% upside) from Rs423/share earlier. Our earlier target price was based on 6-8x FY21E EV/EBITDA, while now it is based on 6-8x FY22E EV/EBITDA. Our target price also factors in:

- Market value of investments in IGL, Petronet LNG and Oil India.
- Book value of oil bonds (GoI bonds).
- Mozambique gas reserves at valuation based on the last deal in the asset. Total bought 26% stake in the asset at US$3.9bn in Sep'19. BPCL holds 10% in this asset, which we have valued at US$1.5bn (Rs108.75bn)
- Oil & gas reserves in Russia (Vankor and Taas-Yuriakh) valued at US$800m (Rs58bn).

**Table 3: 56% of the holding at Rs609/share, balance 44% at Rs462/share**

| **(Rs-mn)** | | |
|---|---|---|
| **FY22E EBITDA** | 1,59,793 | |
| Multiple | 6.0 | 8.0 |
| EV | 9,58,760 | 12,78,347 |
| Less: Net debt | 3,02,285 | 3,02,285 |
| Add; Market value of investments and oil bonds | 1,79,114 | 1,79,114 |
| Value of oil & gas reserves in Mozambique and Russia | 1,66,750 | 1,66,750 |
| **Equity value** | **10,02,339** | **13,21,926** |
| **Fair value (Rs/share)** | **462** | **609** |
| **Outstanding shares** | **2,169** | **2,169** |
| **INR** | **72.5** | |

Source: Company data, I-Sec research

### 56% holding assumed to be sold in open offer; 44% post-open offer

Our target price is based on the assumption that:

- 56% of the holding of an investor is sold in the open offer by the successful bidder in privatisation at Rs609/share; successful bidder is assumed to bid at 8x FY22E EV/EBITDA.
- Balance 44% of the holding is sold in the market after the open offer at Rs462/share (6x FY22E EV/EBITDA).

**Table 4: Target price of Rs544/share assumes open offer at Rs609/share (8x FY22E EV/EBITDA); FV Rs628/share if at Rs759/share (Essar oil deal valuation)**

| | Price realised | | |
|---|---|---|---|
| | In open offer | Post-open offer | Total realisation |
| **Fair Value** | | | |
| Base case fair value (Open offer at 8x FY22 EV/EBITDA) | 609 | 462 | **544** |
| Bull case fair value (Open offer at Essar oil deal based value) | 759 | 462 | **628** |

Source: Company data, I-Sec research

### Upside to FV from higher bid price & higher GRM than estimated

Upside to FV would be:

- 15% at Rs628/share (47% upside) if the successful bidder bids at Rs759/share (BPCL's EV at US$20bn based on Essar Oil deal valuation).
- 11% at Rs606 (42% upside) if FY22E GRM is US$1/bbl higher than our estimate at US$4.5/bbl, which would mean higher bid price as well as market price.

## Risks to recommendation

Risks to our BUY recommendation may be due to:

- BPCL privatisation does not go through. Our fair value if privatisation does not go through is Rs462/share (8% upside).
- Bid by successful bidder in privatisation is sharply lower than our estimate of Rs609/share.
- BPCL's FY22E GRM is lower than our estimate. If its FY22E core GRM is US$2/bbl or lower, our fair value would be lower at Rs451 (6% upside).
- BPCL's FY22E auto fuel net marketing margin is lower than estimated. If its FY22E net auto fuel marketing margin is at Rs1.5-2.0/l, our fair value would be lower at Rs414/share (3% downside) and Rs479/share (12% upside).

## Singapore GRM at 6-quarter high but not out of the woods

### Singapore GRM at 6-quarter high on demand recovery & US freeze

Reuters' Singapore GRM touched a low of minus US$0.93/bbl in Q1FY21 hit by lockdowns due to covid leading to collapse in global oil demand. Singapore GRM is now at 6-quarter high of US$1.9/bbl in Q4FY21-TD driven by:

- Global oil demand recovery from lows in Q1FY21 on gradual lifting of lockdowns and rollout of vaccines.

- US snowstorms in mid-Feb'21 leading to decline in US refinery utilisation to 56-76% in weeks ended 19-Feb'21 to 12-Mar'21 vs 83.1% in week ended 12-Feb'21.

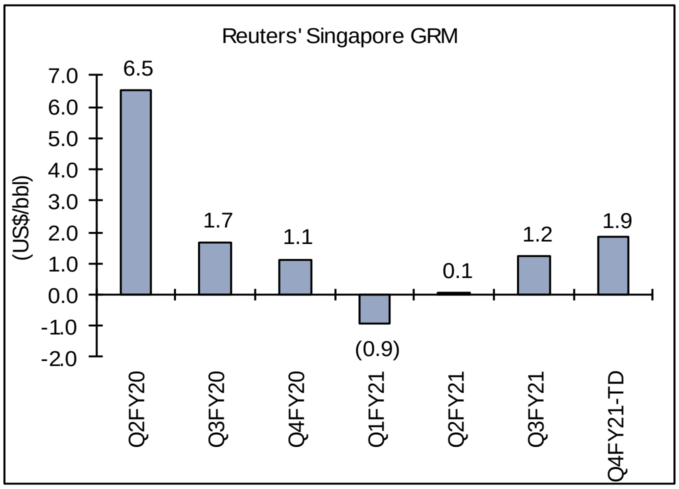
## Global oil demand up 11m b/d from lows in Q1FY21 but down QoQ

As per IEA's Feb'21 Oil Market Report (OMR) global oil demand:

- Bottomed out at 82.9m b/d in Q1FY21.
- Up 11m b/d from Q1FY21 levels to 93.9mb/d in Q4FY21E.

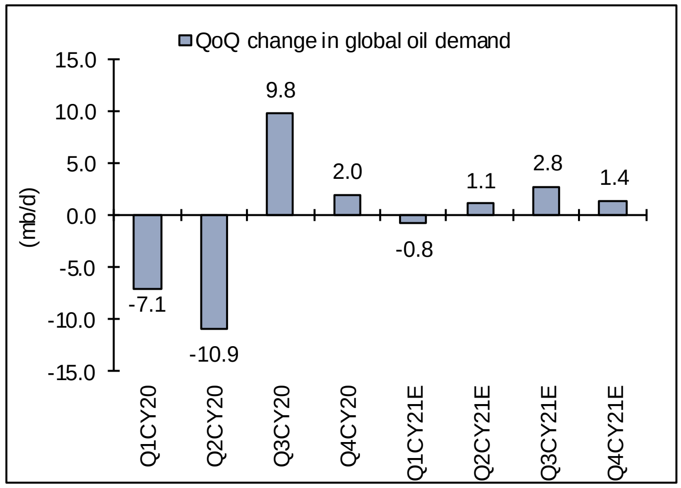
However, global demand in Q4FY21 is down 0.8m b/d from Q3FY21 levels due to second wave of covid hitting demand, especially, in Europe and also due to seasonal factors; seasonally, demand is lower QoQ in Jan-Mar.

**Chart 1: Reuters' Singapore GRM at 6-quarter high of US$1.9/bbl in Q4FY21-TD**




Source: Reuters, I-Sec research

**Chart 2: Global oil demand up 11m b/d in Q1CY21 from lows of Q2CY20 but down QoQ**




Source: IEA, I-Sec research

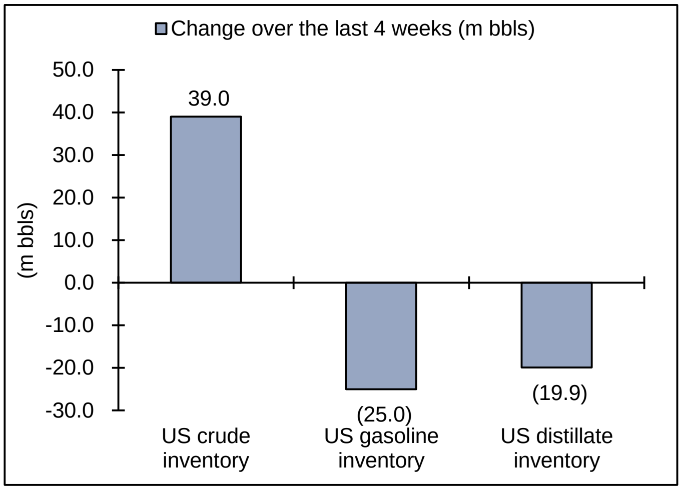
## US petrol & diesel inventory plunge below 5-year lows on snowstorms

Two US snowstorms in the week ended 19-Feb'21 led to shutdown of 4.4m b/d of refining capacity with another 1.5m b/d capacity being partially impacted. US refinery utilisation was down to 76% vs 83% before the snowstorms and US refinery throughput was 1.3m b/d below pre-snowstorm levels in the week ended 12-Mar'21. This means:

- US gasoline inventories are down by 25.0m bbls during week ending 12-Feb'21 to week ending 12-Mar'21.
- US distillate inventories are down by 19.9m bbls during week ending 12-Feb'21 to week ending 12-Mar'21.

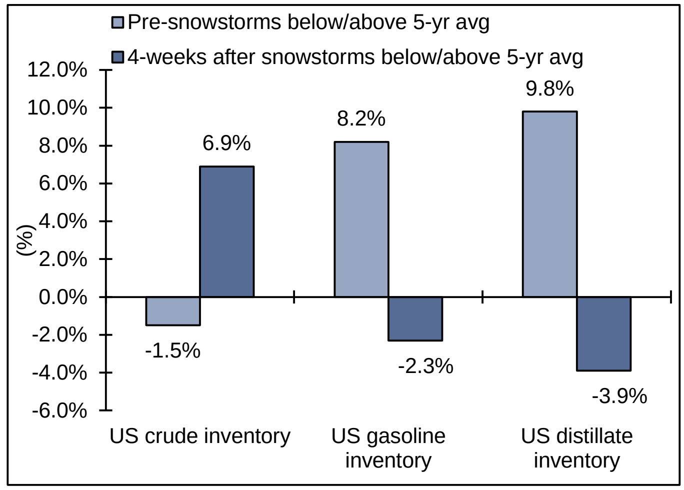
S&P Global Platts estimates 80m bbls of refining throughput loss due to the snowstorms-triggered shutdowns in the four weeks ended 12-Mar'21.

**Chart 3: US oil inventory surged, but that of products plunged as oil recovered before refineries**




Source: EIA, I-Sec research

**Chart 4: Snowstorms dragged US crude stocks above 5-year average & pushed products below**



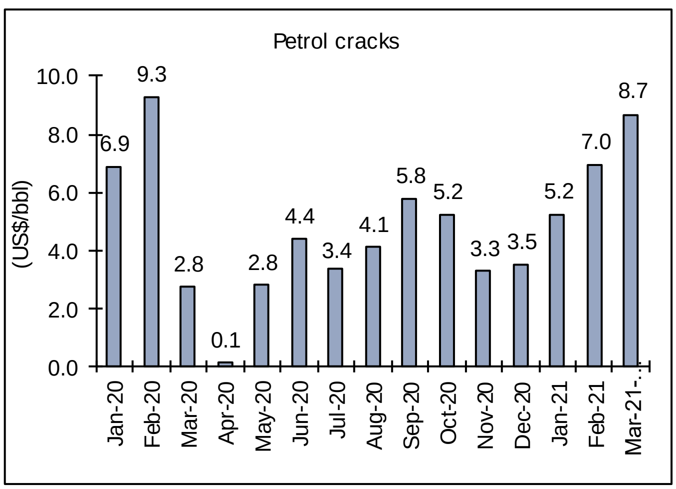

Source: EIA, I-Sec research

## Petrol cracks main driver of GRM rise; at 5-quarter & 13-month high

The main driver of GRM recovery are petrol cracks, which are at a 5-quarter high of US$6.7/bbl in Q4FY21-TD, 13-month high of US$8.7/bbl and at US$9.8/bbl on 17-Mar'21. Petrol cracks recovery appears mainly driven by US snowstorms, which:

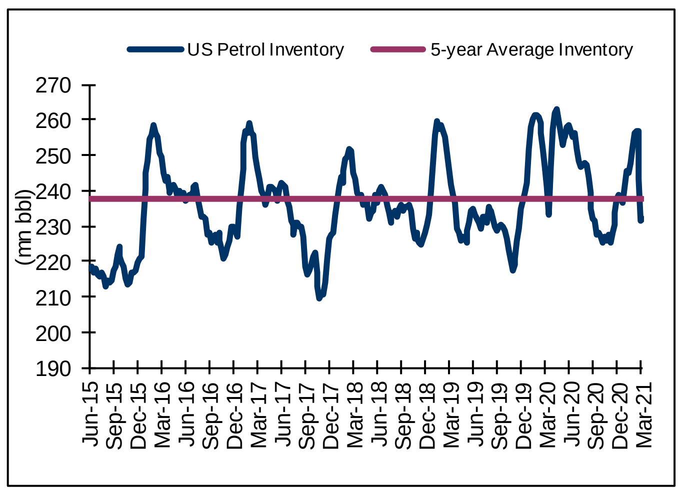
- Led to plunge in US gasoline inventories by 25m bbls over four weeks.
- Pushed US gasoline inventories down from being 8.2% above 5-year average levels pre-snowstorms to 2.3% below 5-year average levels in the week ended 12-Mar'21.

**Chart 5: Petrol cracks at 13-month high of US$8.7/bbl in Mar'21-TD**




Source: Reuters, I-Sec research

**Chart 6: US gasoline inventory 2.3% below 5-year average after 25m bbls fall in last four weeks**



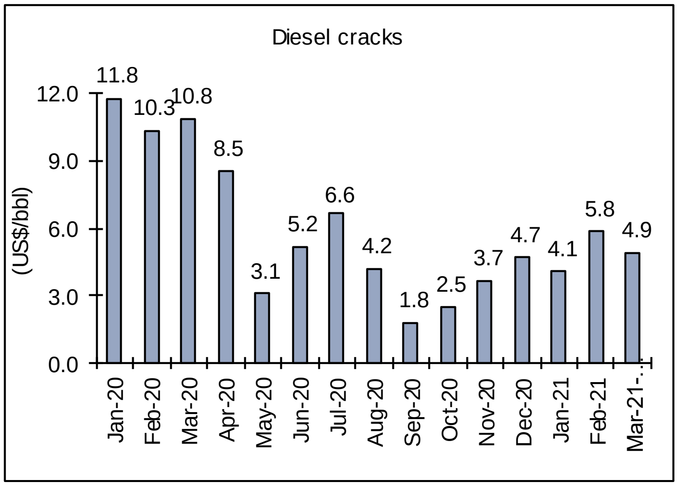

Source: EIA, I-Sec research

## Diesel cracks still weak and well below pre-covid levels

US snowstorms also led to a plunge in US distillate inventories by 19.9m bbls over four weeks. It meant US distillate inventories from being 9.8% above 5-year average levels pre-snowstorms were 3.9% below 5-year average levels in the week ending 12-Mar'21. Diesel cracks, which were at US$5.3/bbl in Feb'21 before the snowstorm, surged to US$7/bbl at peak on 23-Feb'21 and remained at US$5.4/bbl or higher until 4-Mar21 but thereafter, are consistently below US$5/bbl. Diesel cracks were at 7-month high of US$5.8/bbl in Feb'21 but are down to US$4.9/bbl in Mar'21-TD. Diesel cracks are well below:

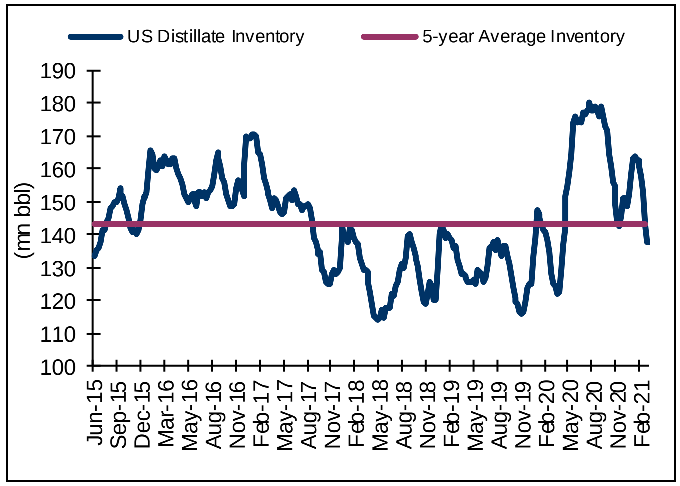
- Pre-covid levels of US$12.4-15.3/bbl in Q1-Q3FY20.
- Even below US$11.3/bbl in Q4FY20 and US$8.5/bbl in Apr'20 in the initial period of the pandemic.

**Chart 7: Diesel cracks at 7-month high of US$5.8/bbl in Feb'21; down MoM in Mar'21-TD**




Source: Reuters, I-Sec research

**Chart 8: US distillate inventory 3.9% below 5-year average after 20m bbls fall in last four weeks**



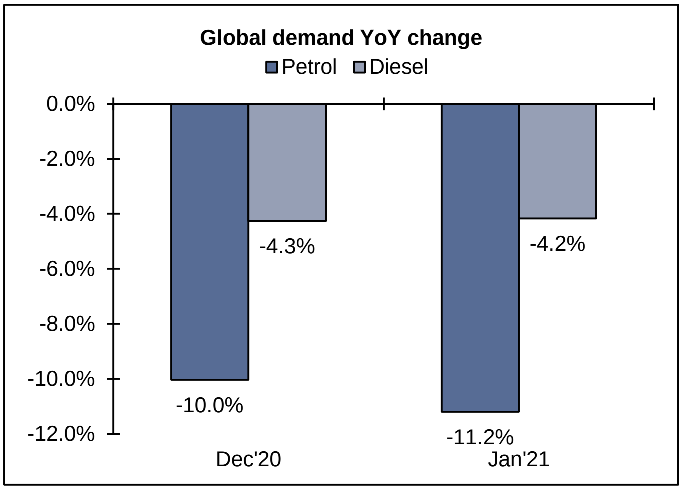

Source: EIA, I-Sec research

## Diesel cracks weak despite strong recovery & sharp inventory fall

Diesel cracks hit a low of US$1.8/bbl in Sep'20, but had recovered to 7-month high of US$5.8/bbl in Feb'21 boosted by US refinery shutdowns. However, as discussed, this recovery petered out within 2 weeks with diesel cracks back to pre-snowstorm levels. Weakness in diesel cracks has persisted while petrol cracks are at a 13-month high in Mar'21-TD despite:

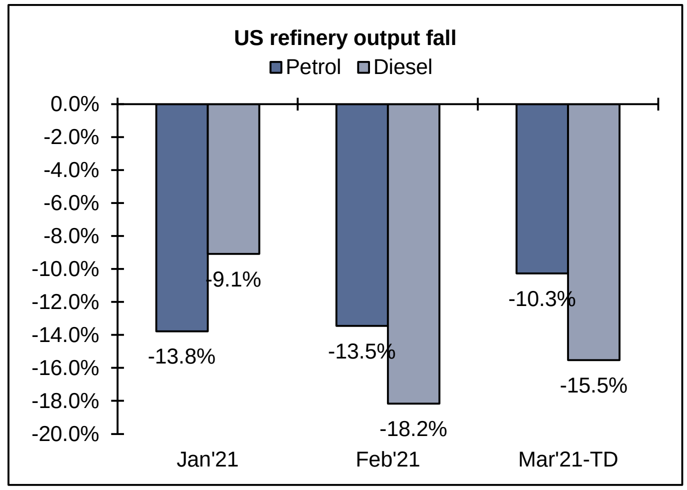
- Diesel demand in countries accounting for 53-27% of global demand, was down just 4.3-4.2% YoY in Dec'20 and Jan'21, respectively, while gasoline's YoY demand decline in countries accounted for 63-40% of global demand, which was steeper at 10.0-11.2% during the same months.
- US distillate inventories are down 13% while gasoline inventories are down 10% from pre-snowstorm levels and diesel inventories are 4.2% below vs 9.8% above whereas US gasoline are 2.5% below vs 8.2% above 5-year average.
- US distillate yield has fallen 0.6-0.7pct points below year-ago levels at 25.3-24.5% in Feb'21-Mar'21-TD; it had surged to 36% in Apr'20 (up 9.6pct points). US gasoline yield on the other hand is 2.4-1.8pct point above year-ago levels at 54.3-55.2% in Feb'21-Mar'21-TD. **The rise in gasoline yield and fall in diesel yield is mainly due to snowstorms, which meant US refinery utilisation was down to 72.7-72.6% in Feb'21-Mar'21-TD vs 78.6% in CY20 and 82.1% in Jan'21. US refineries distillate output fall is steeper at 18-16% YoY vs 13-10% for gasoline in Feb'21-Mar'21-TD. However, in Jan'21 before the snowstorms, US gasoline output fall was steeper at 14% YoY vs 9% for distillates.**

**Chart 9: Diesel demand fall in Dec'20-Jan'21 modest at 4.3-4.2% vs 10-11.2% for gasoline**




Source: JODI, I-Sec research

**Chart 10: US refineries distillate output YoY fall steeper than gasoline in Feb'21-Mar'21-TD**



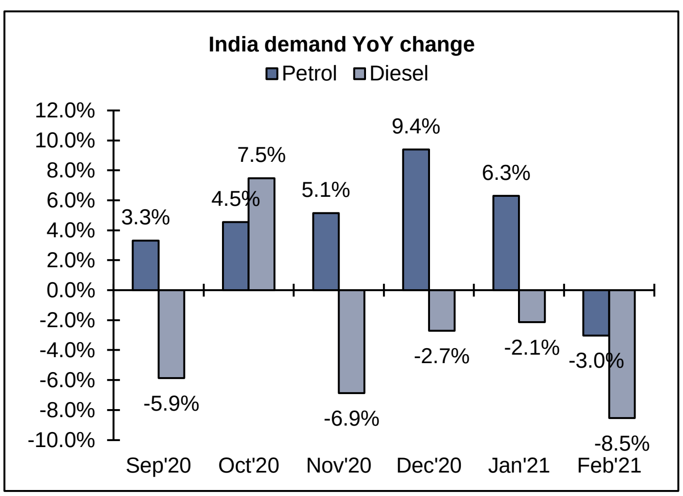

Source: EIA, I-Sec research

## Diesel cracks hit by fall in India/China demand & jump in India exports

Diesel cracks weakness, especially when compared with petrol cracks, is perplexing given the stronger demand recovery in diesel, lower US inventories and lower US supply than in case of petrol. However, some factors that may be hurting diesel cracks are:

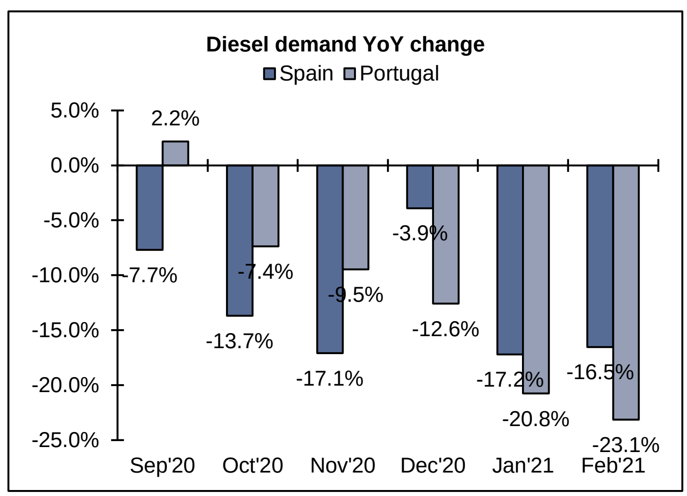
- **Slower demand recovery of diesel than petrol in net exporting countries like China and India.** Chinese diesel demand was down 5% YoY while gasoline was flat YoY in Dec'20. Indian diesel demand is down 2.1-8.5% YoY in Dec'20-Feb'21 while petrol demand was up 6.3-9.4% YoY in Dec'20-Jan'21 and down 3% YoY in Feb'21.

**Chart 11: Diesel demand recovery slower than petrol in India**




Source: PPAC, I-Sec research

**Chart 12: Diesel demand fall in Spain & Portugal (steepest since Apr'20) 16.5-23.1% YoY in Feb'21**

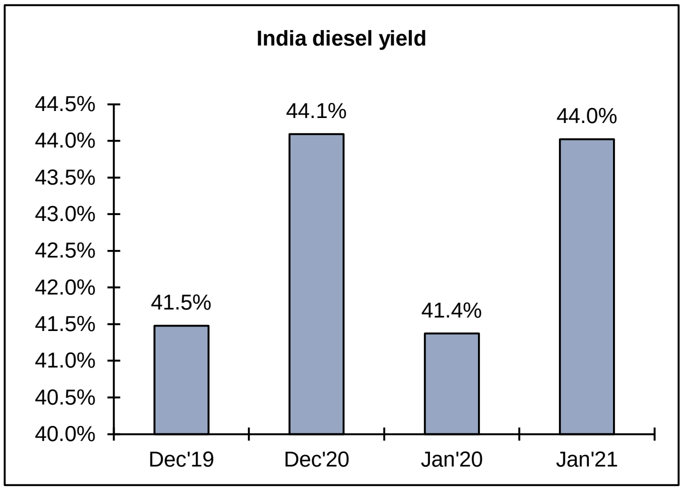



Source: CLH, ENSE, I-Sec research

- **Diesel demand weakness in Europe (second wave), which accounted for 23% of global demand in CY19;** Europe accounted for just 7% of global petrol demand. **Diesel demand in Spain was down 16.5% YoY while that in Portugal was down 23.1% YoY (steepest fall since Apr'21) in Feb'21.**

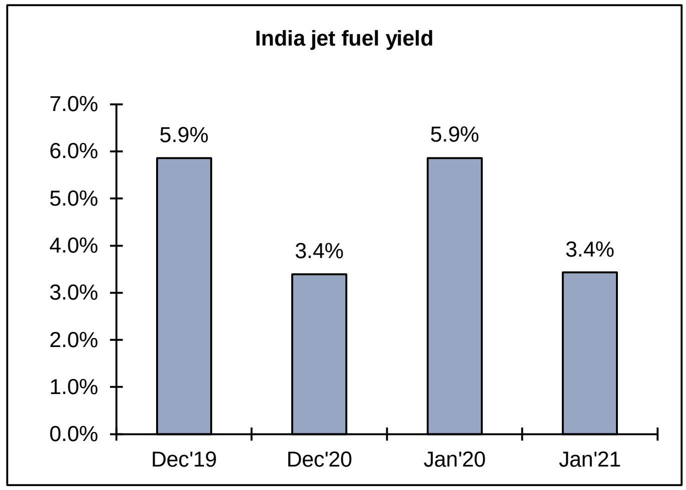
- **India's diesel net exports were up 56% YoY at 2.2mmt in Jan'21.**
- **Continued weakness in jet fuel demand may mean rise in diesel yield for refiners operating at high utilisation rates.** Global jet fuel demand decline is far steeper than auto fuels at 27.3% YoY in Dec'20 and 36.1% YoY in Jan'21. In India, jet fuel demand is down 37-41% YoY vs 2.1-8.5% YoY fall for diesel in in Dec'20-Feb'21. This has meant diesel yield of Indian refiners was up YoY at 44.0-44.1% in Jan'21 and Dec'20 vs 41.4-41.5% in Jan'20 and Dec'19. Jet fuel yield in India is down to 3.4% in Dec'20-Jan'21 vs 5.9% in Dec'19-Jan'20.

**Chart 13: Indian refiners' diesel yield up YoY in Dec'20 and Jan'21**




Source: PPAC, I-Sec research

**Chart 14: Indian refiners' jet fuel yield down YoY in Dec'20 and Jan'21**




Source: PPAC, I-Sec research

## Second wave of covid a headwind to GRM

### GRMs hit as second covid wave in US and Europe hits demand

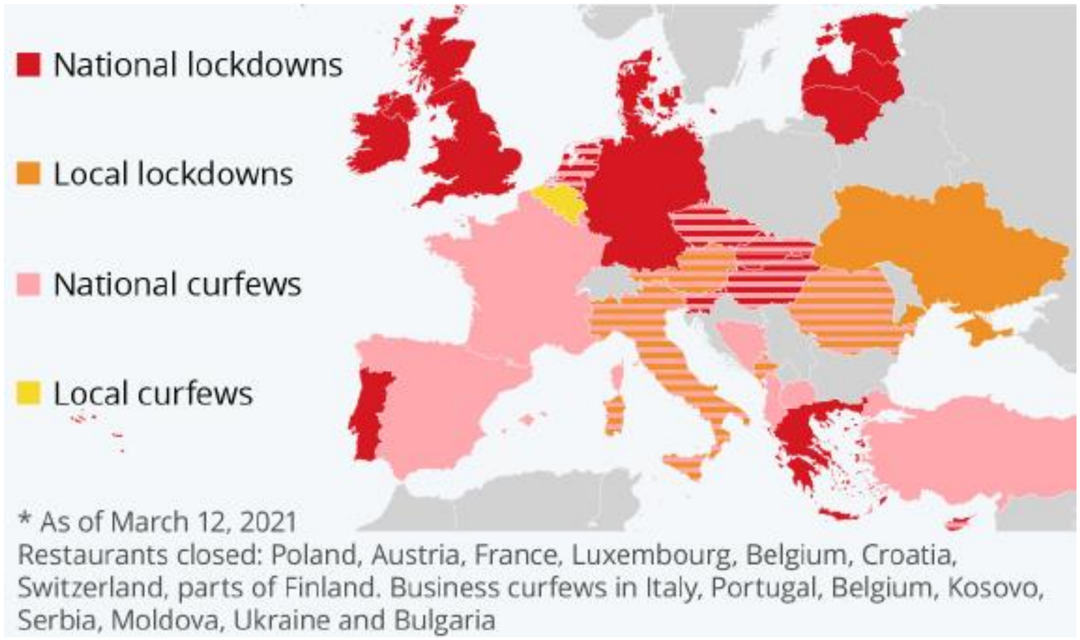
GRMs appear to have been hit by the second wave of covid in US and Europe, which led to dramatic reversal of demand recovery especially in Europe. There is a fear that slow rate of vaccinations may mean third wave of covid in some European countries like Italy and Germany. Demand for auto fuels, which had significantly recovered and in some cases were up YoY in Sep'20, saw steeper declines from Oct'20. Following demand data in Europe is worrying:

- In UK, Spain, Portugal and Italy petrol demand decline in Jan'21 was the steepest since May'20.
- In Portugal petrol and diesel demand decline in Feb'21 is the steepest since Apr'21.

### Spain & Portugal petrol demand down 29-40% & diesel 17-23% in Feb

In Spain petrol demand decline was 29.4% YoY (vs 30.6% YoY in Jan'21) and diesel demand decline 16.5% YoY (vs 17.2% YoY in Jan'21) in Feb'21. Thus, auto fuel demand decline in Spain is marginally more modest in Feb'21 than in Jan'21. However, in Portugal petrol demand decline at 39.7% YoY and diesel demand decline at 23.1% YoY is the steepest since Apr'20.

**Chart 5: European countries in lockdown due to second-wave of covid**



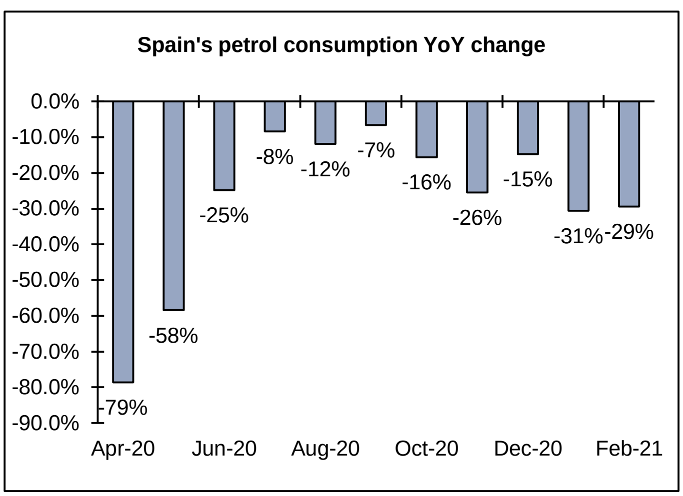

Source: Statista, I-Sec research

## Petrol demand down 31-33% YoY in Jan'21 in Spain, Italy & Portugal

Petrol consumption recovered and was down just 7% YoY in Sep'20 (8-79% YoY fall in Apr-Aug'20) in Spain. In Italy (down 5-73% YoY in Apr-Aug'20) and Portugal (down 9-61% YoY), petrol consumption recovered by 1-3% YoY in Sep'20. However, demand recovery reversed in Oct-Dec'20 and was down 15-26% YoY in Spain, 7-17% in Portugal and 13-28% in Italy. Demand decline in Jan'21 was steepest since May'20 at:

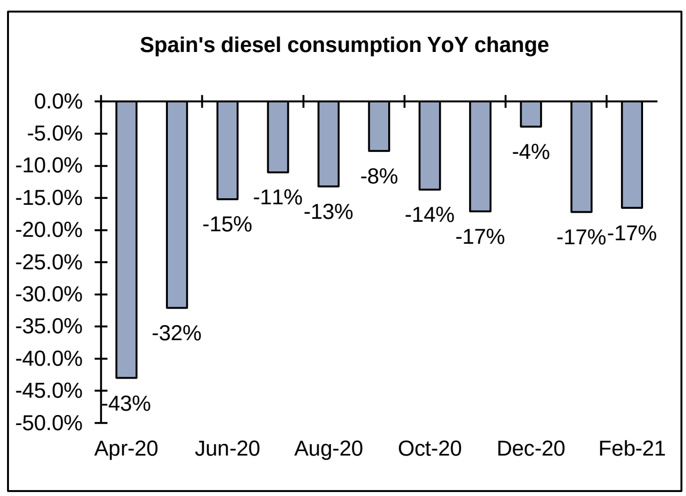
- 30.6% YoY in Spain
- 32% YoY in Italy
- 33% YoY in Portugal

**Chart 15: Spain's petrol consumption down 31% YoY in Jan'21; worst fall since May'20**




Source: CLH, I-Sec research

**Chart 16: Spain's diesel consumption down 17% YoY in Jan'21; worst fall since May'20**

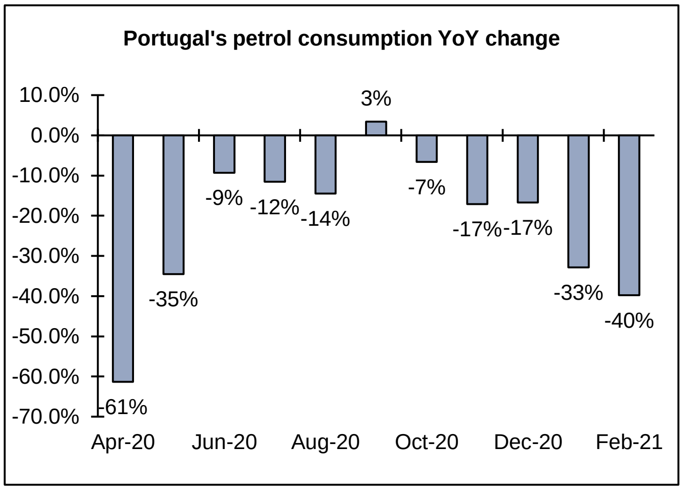



Source: CLH, I-Sec research

## Diesel demand down 17-21% YoY in Jan'21 in Spain, Italy & Portugal

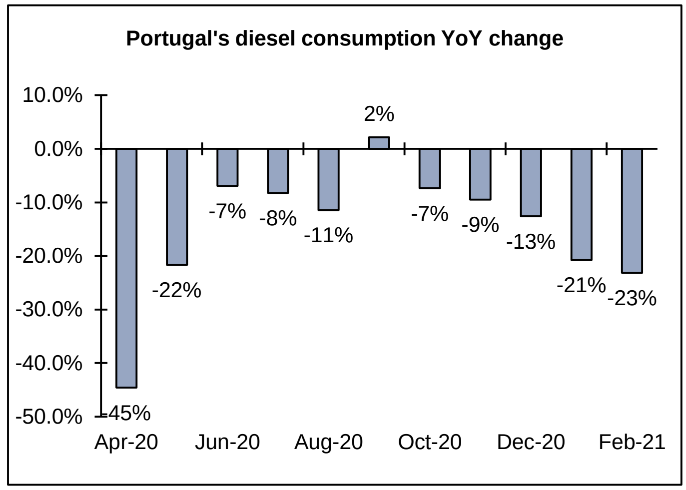
Diesel consumption recovered and was down just 4% YoY in Dec'20 (8-43% YoY fall in Apr-Nov'20) in Spain.

**Chart 17: Portugal's petrol consumption down 40% YoY in Feb'21; worst fall since Apr'20**




Source: ENSE, I-Sec research

**Chart 18: Portugal's diesel consumption down 23% YoY in Feb'21; worst fall since Apr'20**

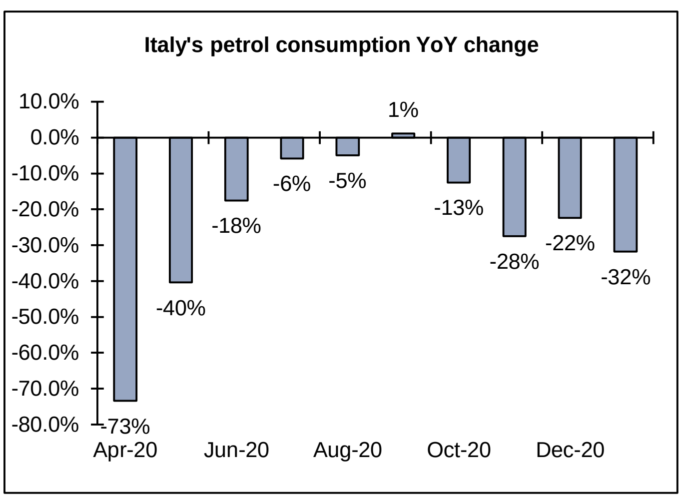



Source: ENSE, I-Sec research

Diesel consumption recovered to be down just 0.4% YoY in Italy (down 6-50% YoY in Apr-Aug'20) in Sep'20 and in Portugal (down 7-45% YoY in Apr-Aug'20) to be up 2% YoY in Sep'20. However, demand recovery reversed in Oct-Dec'20 to be 7-13% in Portugal and 11-12% in Italy. Demand decline was steeper (steepest since May'20) in Jan'21 at:

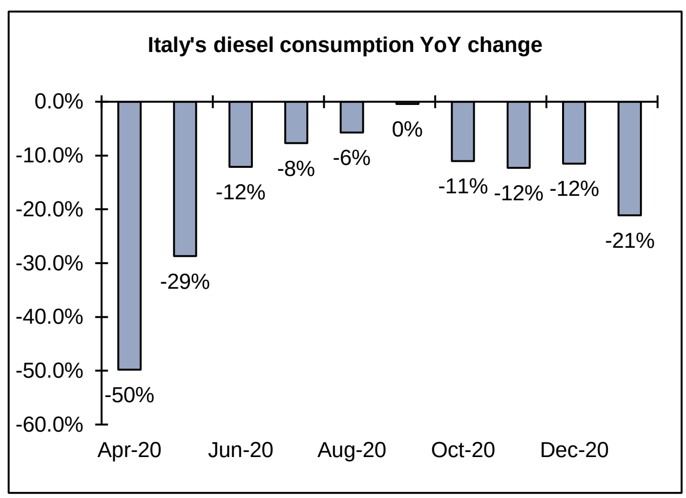
- 17.2% YoY in Spain
- 21% YoY in Italy
- 21% YoY in Portugal

**Chart 19: Italy's petrol consumption down 32% YoY in Jan'21; worst fall since May'20**




Source: MoED Italy, I-Sec research

**Chart 20: Italy's diesel consumption down 21% YoY in Jan'21; worst fall since May'20**




Source: MoED Italy, I-Sec research

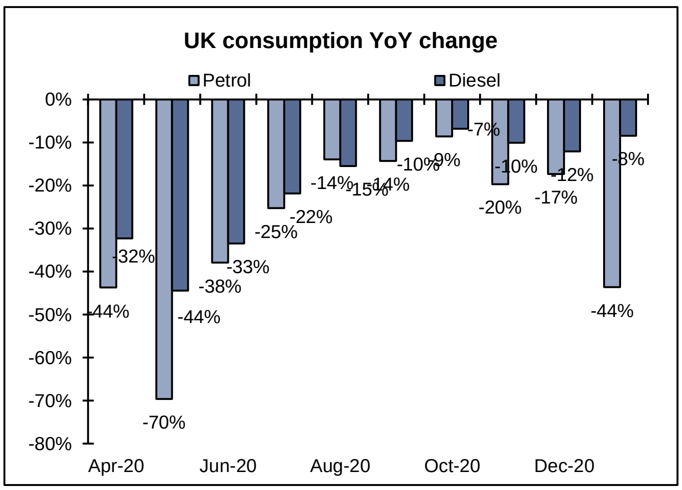
## Petrol demand in Germany down 32% YoY in Dec'20

Petrol consumption in Germany was down 32% YoY in Dec'20 vs 1-29% YoY fall in Apr-Nov'20. Diesel consumption in Germany was down 7% YoY in Dec'20 vs 1-20% YoY decline in Jun-Nov'20 with decline being steepest in Aug'20.

## Petrol demand in UK down 44% YoY in Jan'21; fall may be 40% in Feb

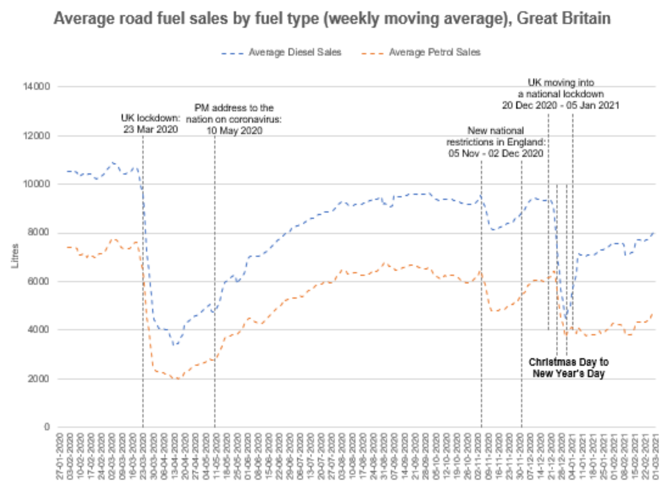
UK diesel consumption was down 8% YoY and petrol consumption down 44% YoY in Jan'21. Second wave of covid led to imposition of level four lockdown in the UK from 25-Dec'20 to 4-Jan'21 and imposition of nationwide lockdown from 5-Jan'21. Data from UK fuel sales at sampled stations indicates that the fall in demand was much steeper in Jan'21 than in Dec'20, but may have recovered in Feb'21. We estimate diesel and petrol demand decline at 2-40% YoY in Feb'21.

**Chart 21: UK diesel and petrol demand decline at 8-44% YoY in Jan'21**




Source: Department of Energy UK, I-Sec research

**Chart 22: UK diesel and petrol demand fall may be 2-40% YoY in Feb'21 as per sampled station sales**




Source: Department of Energy UK, I-Sec research

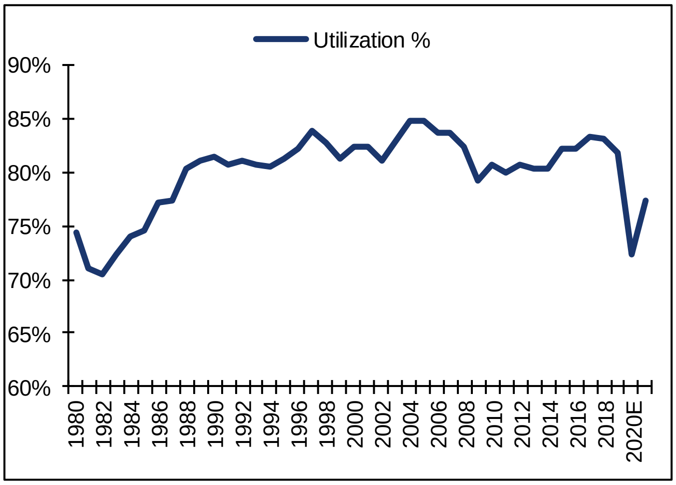
# Vaccine-driven demand rise and refinery closure to boost GRMs

## GRMs to be up YoY as vaccines boost demand and capacity is shut

Recovery in global oil demand, decline in bloated product inventories and closure of refineries to reduce refining overcapacity are key to GRM recovery. We expect GRM to be up YoY in CY21E/FY22E driven by:

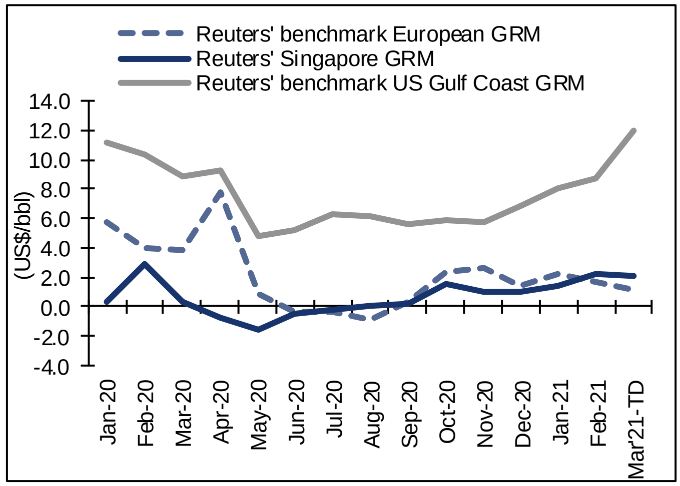
- Gradual vaccine rollout globally, which is expected to boost global oil demand. IEA estimates global oil demand, which is down 9M b/d YoY in CY20E, to be up 5.4m b/d YoY in CY21E.
- Decline in US gasoline and diesel inventories. As discussed, US snowstorms in Feb'21 have led to refinery closures and steep decline in gasoline and distillate inventories to 2.3-3.9% below 5-year average levels.
- Permanent closure of refining capacity helps boost global refinery utilisation to 77.4% in CY21E from 38-year low of 72.4% in CY20E. We estimate permanent closure of 1.5m b/d refining capacity globally in CY20-CY21E. Permanent closure of another 1.4m b/d of capacity is under consideration.

**Chart 23: Global refinery utilisation to rise to 77.4% in CY21E from 38-year low of 72.4% in CY20**




Source: EIA, IEA, Wood Mackenzie, I-Sec research

**Chart 24: US snowstorms drive up US GRM to 16-month high; Europe GRM lag hit by second wave**




Source: Reuters, I-Sec research

## Permanent closure of 1.5m b/d capacity likely in CY20-CY21E

GRMs in CY20E are hit by a decline in global refinery utilisation to 72.4%, which is the lowest level in 38 years due to steep decline in global demand. Low GRMs and fall in demand is making it unviable for refineries to operate as a result of which 1.5m b/d refining capacity in US, Japan, Philippines, Finland and France may be shut in CY20-21, out of which 0.4m b/d capacity would have been converted for biodiesel. Moreover, potential closure of another 1.4m b/d refining capacity in Europe, Australia, New Zealand and Philippines is under consideration.

**Table 6: 1.5m b/d refining capacity may be shut in CY20-21; closure of another 1.4m b/d possible**

| Refinery | Country | Capacity (k b/d) |
|---|---|---|
| **Refinery shutdowns** | | |
| Royal Dutch Shell | Philippines | 110 |
| Royal Dutch Shell | Louisiana, USA | 240 |
| Marathon Petroleum | USA | 161 |
| Marathon Petroleum | USA | 26 |
| Neste | Finland | 58 |
| JXTG | Japan | 115 |
| BP | Kwinana, Australia | 146 |
| Irving Oil | Newfoundland | 135 |
| PBF | Paulsboro, NJ | 85 |
| **Sub-total** | | **1,076** |
| **Shutdown and conversion to biodiesel** | | |
| Holly Frontier | USA | 48 |
| Neste | Finland | 240 |
| Total | France | 101 |
| **Sub-total** | | **389** |
| **Total refinery closures** | | **1,465** |
| **Potential Closures** | | |
| Gunvor Group | Belgium | 110 |
| BP | Netherlands | 377 |
| Petroineos | UK | 200 |
| Viva | Australia | 120 |
| New Zealand refining NZ | New Zealand | 135 |
| Petron | Philippines | 180 |
| Phillips 66 | Santa Maria, CA, USA | 44.5 |
| Calcasieu Refining | Lake Charles, LA | 136 |
| Phillips 66 | Rodeo, CA, USA | 120 |
| Phillips 66 | USA | 19 |
| **Sub-total** | | **1,441** |
| **Total closures and potential closures** | | **2,906** |

Source: Industry data, I-Sec research

## Marketing margin at minus Rs0.16/l if no price hike or excise cut

### Net marketing margin at Rs3.19/l in FY21-TD and Rs0.09/l now

Auto fuel net marketing margin is:

- Rs3.19/l in FY21-TD.
- Rs1.36/l in Q4FY21-TD.
- Rs0.09/l on 18-Mar'21.

### Net margin in Mar'21-TD at Rs0.81/l, lowest in FY21-TD

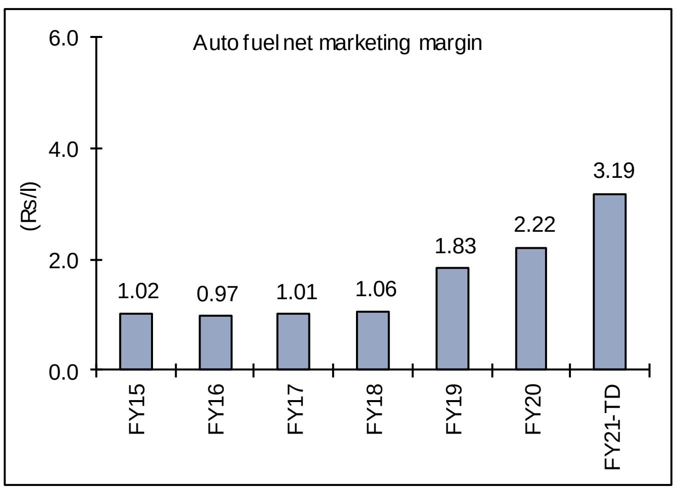
The rise in international auto fuel prices has not been passed on to consumers in Mar'21-TD. It has led to a decline in auto fuel net marketing margin from Rs3.47/l during 7-15 Dec'20 to just Rs0.09 on 18-Mar'21 and net margin being the lowest in FY21-TD at just Rs0.81/l in Mar'21-TD.

### Margin to fall to minus Rs0.16/l on 1-Apr unless price hiked/excise cut

Continued rise in international auto fuel prices and domestic prices not keeping pace has led to net marketing margin falling to Rs0.09/l on 18-Mar'21. If no retail price hikes or excise duty cuts are made and not passed-on fully to consumers, we estimate net margin at:

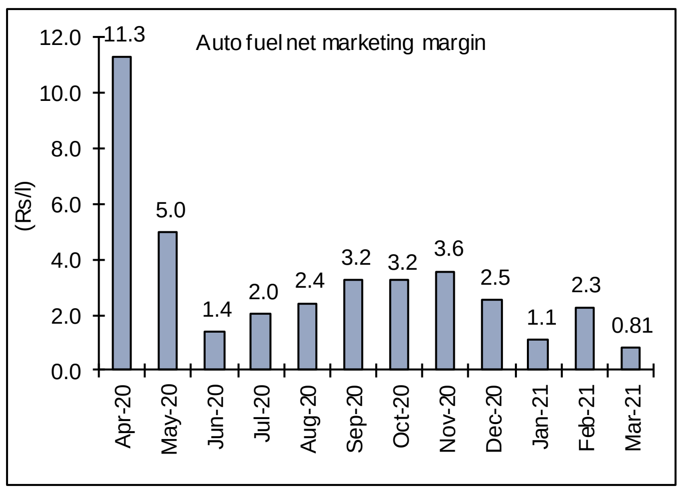
- Minus Rs0.16/l on 1-Apr'21 based on international prices in 16-17 Mar'21.
- Minus Rs0.22/l on 16-Apr'21 at latest international and domestic prices (17-Mar'21).

**Chart 25: OMCs' auto fuel net marketing margin is Rs3.19/l in FY21-TD vs Rs2.22/l in FY20**




Source: PPAC, Reuters, I-Sec research

**Chart 26: OMCs' net margin at Rs0.81/l in Mar'21-TD is lowest in FY21-TD**




Source: PPAC, Reuters, I-Sec research

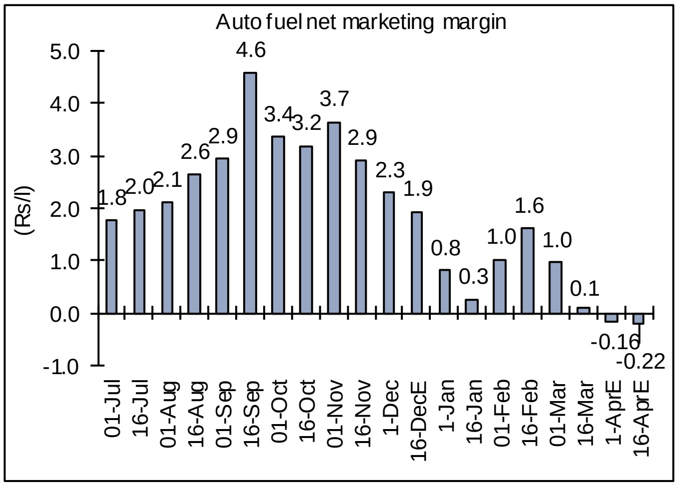
### Rs3.15/l price hike needed to boost net margin to ~Rs2.5/l on 1-Apr

Retail price hikes worth Rs3.15/l are required for net margins to be over Rs2.5/l on 1-Apr'21. It would also mean FY21E net margin is Rs3.14/l. If no further retail price hikes are made and international prices remain at current levels, FY21E net auto fuel marketing margin will be lower at Rs3.07/l.

### FY21E net margin up 38% YoY at Rs3.07/l despite no price hikes

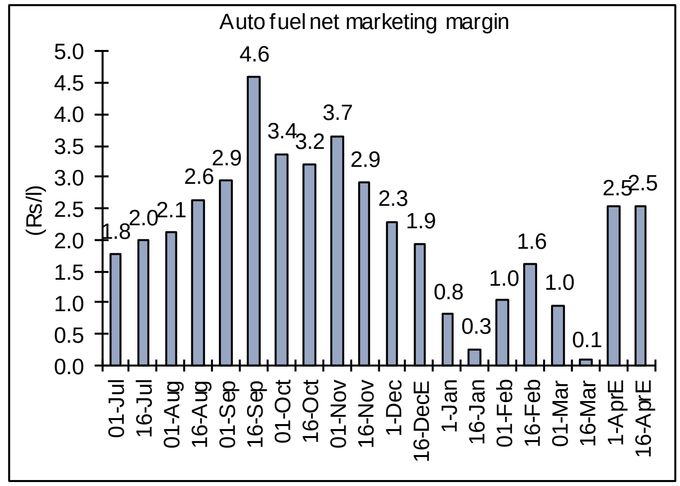
FY21E net margin will be Rs3.07/l even if net margin is Rs0.09/l for the rest of FY21. OMCs' FY21E EPS is also likely to be up sharply YoY. We estimate BPCL's FY21E EPS to be up 250% YoY driven by YoY higher marketing margins and hefty inventory gains.

**Chart 27: OMCs' net margin in the red on 1-Apr and 16-Apr'21 if no price hikes or excise cut**




Source: PPAC, Reuters, I-Sec research

**Chart 28: Net margin at Rs2.54 on 1-Apr & at latest prices if price hiked by Rs3.15/l or excise cut**




Source: PPAC, Reuters, I-Sec research

## Optimistic on FY22E net margin at Rs2.5/l; excise cut/price hike

### Expect net margin at Rs2.5/l in FY22E given GoI track record

We are optimistic that net marketing margin will rise to Rs2.5/l in FY22E given this government's track record:

- During the first four years of the current government (FY15-FY18), net marketing margin was Rs0.96-1.07/l.
- In the next two years (FY19-FY20), it was higher at Rs1.83-2.22/l.
- Net margin is likely to be YoY higher in FY21E to make up for very weak GRMs.
- Price hikes were made to keep net margins at reasonable levels even when Brent surged to US$86/bbl and INR weakened to 75 to the US$ in Oct'18, seven months before 2019 elections.

**Net margin rise will require either price hikes and/or excise duty cuts that are not passed on.**

### GoI is considering excise duty cuts as per press reports

Petrol and diesel prices have been hiked by Rs7.6-7.7/l (9-10%) in Q4FY21-TD, but still net margin will fall in the red at minus Rs0.16/l on 1-Apr'21 unless retail prices are hiked by another Rs3.15/l. GoI needs to either hike retail price adequately or cut excise duty and not pass on the benefit to consumers leading to hike in OMCs' marketing margin. Excise duty was raised by Rs13-16/l on petrol and diesel via hikes in Mar'20 and May'20 and now stands at Rs31.8/l on diesel and Rs32.9/l on petrol after the changes in excise duty structure in Feb'21 budget. Press reports suggest GoI is considering a cut in excise duty.

### Excise cut of Rs3.15/l not passed on to boost net margin to Rs2.54/l

A cut in excise duty of Rs3.15/l on or before 1-Apr'21, which is not passed on to consumers, would also boost net marketing margin to Rs2.54/l on 1-Apr'21.

## Fiscal math leaves room for excise cut of up to Rs8.5/l

### Excise cut optimism due to volume recovery, inflation & privatisation

We are optimistic on excise duty cuts given:

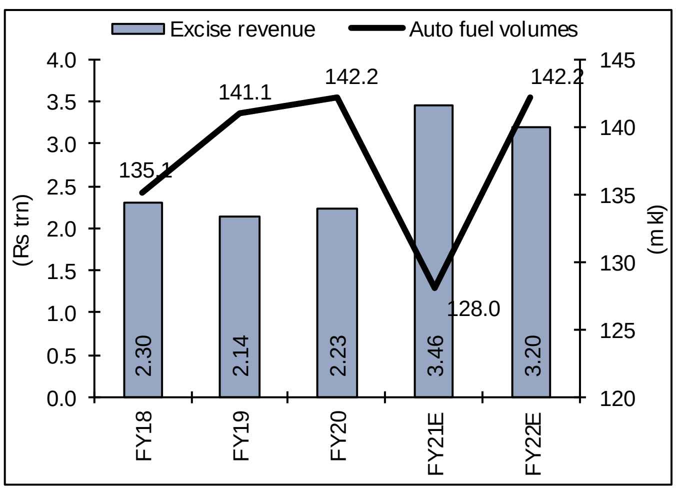
- Budget estimate of excise duty leaves room for excise duty cut of up to Rs8.5/l on or before 1-Apr'21.
- Inflation is a concern.
- Net marketing margins recovering to Rs2.5/l may be key to GoI realising high price for stake sale in BPCL's privatisation.

### FY21E excise revenue likely to exceed revised budget estimate

GoI's revenue from excise duty on auto fuels is:

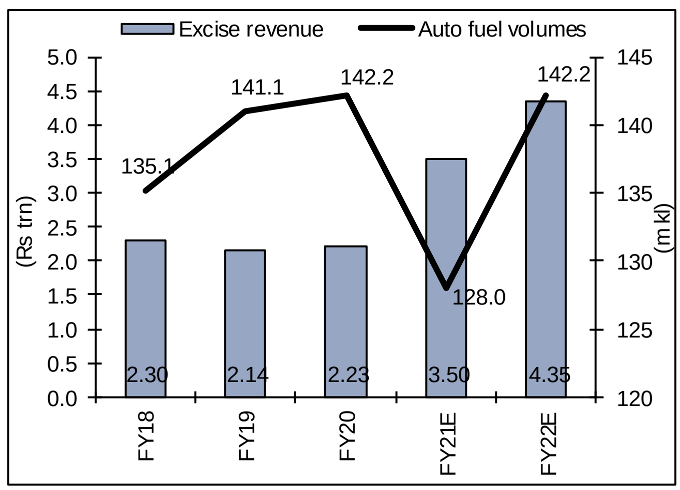
- Rs1.32trn in H1FY21 when petrol volume was down 20.8% YoY and diesel down 25.3% YoY.
- Rs1.04trn in Q3FY21 when petrol volume was up 6.3% YoY but diesel down 1.1% YoY.
- Rs2.36trn in 9MFY21 when petrol volume was down 11.8% YoY and diesel down 17% YoY.

**Chart 29: Budget estimate of excise duty on auto fuels at Rs3.46trn in FY21E and Rs3.2trn in FY22E**




Source: PPAC, Ministry of Finance, I-Sec research

**Chart 30: Excise on auto fuels would be Rs3.5trn in FY21E & Rs4.35trn in FY22E if excise duty not cut**




Source: PPAC, Ministry of Finance, I-Sec research

We estimate excise collection at Rs1.14trn in Q4FY21E and Rs3.5trn in FY21E (vs revised budget estimate of Rs3.46trn) assuming petrol and diesel volume fall 7-11.9% YoY and no excise duty is cut until the end of the year.

## FY22E budget estimate of excise on auto fuels down 8% YoY

Budget estimate of excise duty on auto fuels in FY22E at Rs3.2trn is down 8% YoY vs FY21 revised estimate of Rs3.46trn. Agriculture infrastructure and development cess (AIDC) of Rs2.5-4.0/l was imposed on petrol and diesel, respectively in Budget 2021, while road & infrastructure cess and even basic excise duty was cut to keep total excise duty on auto fuels largely unchanged. We estimate AIDC to boost FY22E excise revenue by Rs505bn assuming FY22E auto fuel volumes are back to FY20 level, implying 11% YoY rise. Finance minister Nirmala Sitharaman, in a press conference, estimated it at Rs300bn. However, AIDC has not been provided in FY22 budget estimates while FY22E budget estimate of road and infrastructure cess on auto fuels at Rs1.98trn is down 12% YoY and basic excise duty in FY22 budget estimate at Rs475bn is down 1% YoY.

**Table 7: FY22E excise duty budget estimate down 8% YoY**

| Rs bn | FY20 | FY21 BE | FY21 RE | FY22 BE | YoY chg |
|---|---|---|---|---|---|
| Basic excise duties | 618 | 824 | 478 | 475 | -1% |
| Additional duty of excise on petrol | 148 | - | - | - | |
| Additional duty of excise on diesel | 407 | - | - | - | |
| Special additional excise duty on petrol | 382 | 405 | 744 | 744 | 0% |
| Road & infrastructure cess | 674 | 1,256 | 2,240 | 1,980 | -12% |
| **Excise duty** | **2,228** | **2,485** | **3,461** | **3,199** | **-8%** |

Source: Ministry of Finance, I-Sec research

## FY22E excise duty on auto fuels at Rs4.35trn if no excise duty cuts

We estimate excise duty on auto fuels in FY22E at Rs4.35trn if:

- FY22E auto fuel volumes are back to FY20 levels.
- There is no excise duty cut on auto fuels throughout FY22E.

In this scenario of no excise duty cuts, we estimate FY22E excise duty on auto fuels at Rs4.35trn to be:

- 36% higher than budget estimate of Rs3.2trn.
- 26% YoY higher vs FY21 revised estimate of Rs3.46trn.

**Table 8: FY22E excise duty on auto fuels to be 36% higher than budget estimate if no cut; same as budget estimate if excise cut by Rs8.5/l on or before 1-Apr'21**

| | FY22E auto fuel sales | FY22E excise duty (Rs/l) | | FY22E excise duty (Rs-bn) | |
|---|---|---|---|---|---|
| | m kl | If no cut | Rs8.5/l cut | If no cut | Rs8.5/l cut |
| Petrol | 42.3 | 32.98 | 24.45 | 1,325 | 982 |
| Diesel | 99.9 | 31.83 | 23.35 | 3,021 | 2,216 |
| Auto fuels | 142.2 | | | **4,347** | **3,199** |
| FY22E budget estimate of excise duty on auto fuels | | | | 3,199 | 3,199 |
| FY22E excise duty on auto fuels vs budget estimate | | | | 36% | 0% |

Source: Ministry of Finance, I-Sec research

## FY22E budget math leaves room to cut excise by Rs8.5/l by 1-Apr'21

FY22E budget auto fuel excise duty estimate of Rs3.2trn leaves room for cut in excise duty by Rs8.5/l on or before 1-Apr'21. Thus, even if excise duty is cut by Rs8.5/l on or before 1-Apr'21, we estimate FY22E excise duty on auto fuels to be in-line with budget estimate. If the cut is more modest, which we expect, FY22E excise duty will be higher than the budget estimate.

# Financial summary

## Table 9: Profit & loss statement

*(Rs mn, year ending March 31)*

| | FY19 | FY20 | FY21E | FY22E |
|---|---|---|---|---|
| **Op. Income (Sales)** | **34,08,792** | **32,97,972** | **23,09,852** | **34,11,328** |
| **Operating Expenses** | **32,57,669** | **32,14,481** | **20,92,500** | **32,51,535** |
| **EBITDA** | **1,51,122** | **83,490** | **2,17,352** | **1,59,793** |
| *% margins* | 4.4% | 2.5% | 9.4% | 4.7% |
| Depreciation & Amortisation | -34,178 | -40,801 | -43,002 | -50,683 |
| Gross Interest | -17,640 | -26,370 | -14,829 | -18,376 |
| Other Income | 20,375 | 19,293 | 27,163 | 26,053 |
| **Recurring PBT** | **1,19,681** | **35,613** | **2,68,716** | **1,16,787** |
| Less: Taxes | 75,905 | 29,458 | 2,10,804 | 84,371 |
| **Net Income (Reported)** | **78,023** | **30,554** | **2,09,447** | **97,071** |
| **Recurring Net Income** | **78,023** | **37,360** | **1,27,414** | **97,071** |

Source: Company data, I-Sec research

## Table 10: Balance sheet

*(Rs mn, year ending March 31)*

| | FY19 | FY20 | FY21E | FY22E |
|---|---|---|---|---|
| **Assets** | | | | |
| Total Current Assets | 5,41,907 | 3,97,244 | 4,33,907 | 5,02,372 |
| *of which cash & cash eqv.* | 6,625 | 11,648 | 1,35,266 | 21,662 |
| Total Current Liabilities & Provisions | 4,63,891 | 4,44,628 | 5,08,352 | 5,52,507 |
| **Net Current Assets** | **78,016** | **-47,384** | **-74,445** | **-50,135** |
| **Investments** | **1,91,078** | **1,05,109** | **1,16,332** | **1,09,157** |
| **Net Fixed Assets** | **5,56,764** | **8,17,067** | **7,05,451** | **7,37,059** |
| *Capital Work-in-Progress* | 72,929 | 1,77,567 | 1,31,711 | 1,78,961 |
| **Total Assets** | **9,05,413** | **10,64,008** | **10,14,314** | **9,96,704** |
| | | | | |
| **Liabilities** | | | | |
| **Borrowings** | **4,29,145** | **6,16,482** | **3,35,551** | **3,28,482** |
| Equity Share Capital | 19,669 | 19,669 | 19,669 | 19,669 |
| *Face Value per share (Rs)* | 10.0 | 10.0 | 10.0 | 10.0 |
| Reserves & Surplus | 3,11,634 | 2,85,928 | 4,95,008 | 5,55,220 |
| **Net Worth** | **3,87,647** | **3,65,323** | **5,82,329** | **6,06,532** |
| **Total Liabilities** | **9,05,413** | **10,64,008** | **10,14,314** | **9,96,704** |

Source: Company data, I-Sec research

## Table 11: Quarterly trend

*(Rs bn, year ending March 31)*

| | Mar'20 | Jun'20 | Sep'20 | Dec'20 |
|---|---|---|---|---|
| Net sales | 813.0 | 506.2 | 659.1 | 865.8 |
| *% growth (YoY)* | (3) | (41) | (12) | 1 |
| EBITDA | (6.2) | 39.2 | 44.8 | 43.8 |
| EBITDA Margin (%) | (0.8) | 7.7 | 6.8 | 5.1 |
| Other income | 11.6 | 5.9 | 5.7 | 15.1 |
| Extraordinary items | (12.7) | - | 7.6 | (4.9) |
| Net profit | (0.9) | 20.8 | 30.0 | 32.7 |

Source: Company data, I-Sec research

## Table 12: Cashflow statement

*(Rs mn, year ending March 31)*

| | FY19 | FY20 | FY21E | FY22E |
|---|---|---|---|---|
| **Operating Cashflow** | **1,10,083** | **70,259** | **2,53,806** | **1,35,055** |
| Working Capital Changes | 61,650 | (1,25,400) | (27,061) | 24,310 |
| **Operating Cashflow** | **48,433** | **1,95,659** | **2,80,867** | **1,10,745** |
| Capital Commitments | (57,921) | (2,25,206) | (25,298) | (1,15,536) |
| **Cashflow from Investing Activities** | **(4,930)** | **(1,39,237)** | **(36,520)** | **(1,08,361)** |
| Inc (Dec) in Borrowings | 59,172 | 1,87,337 | (2,80,931) | (7,069) |
| Dividend paid | 28,830 | 6,653 | 70,929 | 31,796 |
| **Cashflow from Financing Activities** | **30,343** | **1,80,684** | **(3,51,860)** | **(38,865)** |
| **Chg. in Cash & Bank balances** | **73,845** | **2,37,106** | **(1,07,513)** | **(36,481)** |

Source: Company data, I-Sec research

## Table 13: Key ratios

*(Year ending March 31)*

| | FY19 | FY20 | FY21E | FY22E |
|---|---|---|---|---|
| **Per Share Data (Rs)** | | | | |
| EPS (Basic Recurring) | 39.7 | 16.8 | 58.7 | 44.7 |
| Diluted Recurring EPS | 39.7 | 16.8 | 58.7 | 44.7 |
| Recurring Cash flow per share | 56.0 | 35.7 | 117.0 | 62.3 |
| Dividend per share (DPS) | 13.0 | 3.0 | 29.0 | 13.0 |
| Book Value per share (BV) | 197.1 | 185.7 | 268.4 | 279.6 |
| | | | | |
| **Growth Ratios (%)** | | | | |
| Operating Income | 22.0% | -3.3% | -30.0% | 47.7% |
| EBITDA | -0.4% | -44.8% | 160.3% | -26.5% |
| Recurring Net Income | -13.4% | -52.1% | 241.0% | -23.8% |
| Diluted Recurring EPS | -13.4% | -57.7% | 250.0% | -23.8% |
| Cash flow per share | -3.3% | -36.2% | 227.5% | -46.8% |
| | | | | |
| **Valuation Ratios (x)** | | | | |
| P/E | 10.8 | 25.4 | 7.3 | 9.5 |
| P/CEPS | 7.6 | 12.0 | 3.6 | 6.9 |
| P/BV | 2.2 | 2.3 | 1.6 | 1.5 |
| EV / EBITDA | 8.7 | 23.3 | 5.1 | 8.8 |
| EV / Operating Income | 6.8 | 8.7 | 23.3 | 5.1 |
| | | | | |
| **Operating Ratios** | | | | |
| Other Income / PBT (%) | 17.0% | 54.2% | 10.1% | 22.3% |
| Effective Tax Rate (%) | 36.6% | 17.3% | 21.6% | 27.8% |
| NWC / Total Assets (%) | 8.6% | -4.5% | -7.3% | -5.0% |
| D/E Ratio (%) | 110.7% | 168.7% | 57.6% | 54.2% |
| | | | | |
| **Return/Profitability Ratios (%)** | | | | |
| Recurring Net Income Margins | 2.3% | 1.1% | 5.5% | 2.8% |
| RoCE | 15.1% | 4.7% | 18.4% | 11.8% |
| RoNW | 20.7% | 8.1% | 44.2% | 16.3% |
| Dividend Payout Ratio | 36.2% | 35.4% | 30.2% | 30.6% |
| Dividend Yield | 3.0% | 0.7% | 6.7% | 3.0% |
| EBITDA Margins | 4.4% | 2.5% | 9.4% | 4.7% |

Source: Company data, I-Sec research

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